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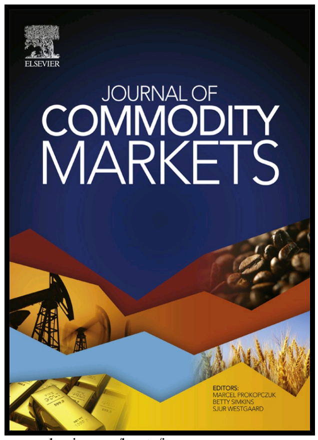
Marco J. Lombardi, Francesco Ravazzolo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# On the correlation between commodity and equity returns: implications for portfolio allocation *

Marco J. Lombardi† Francesco Ravazzolo‡

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**Abstract**

In recent years several commentators hinted at an increase of the correlation between equity and commodity returns, blaming for that surging investment in commodity-related products. This paper investigates such claims by looking at various measures of correlation, and assesses what are the implications of this for asset allocation. We develop a time-varying Bayesian Dynamic Conditional Correlation model and find that joint modelling commodity and equity prices produces accurate forecasts, which lead to benefits in portfolio allocation. This, however, comes at the price of higher volatility. Therefore, the popular view that commodities are to be included in investment portfolio as hedging device is not grounded.

**Keywords:** Commodity prices, equity prices, correlation, Bayesian DCC, multi asset class investment.

**JEL Classification :** C11, C15, C53, E17, G11.

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†Bank for International Settlements. Email: marco.lombardi@bis.org

‡Free University of Bozen-Bolzano and BI Norwegian Business School. Email: francesco.ravazzolo@unibz.it